September 2009

National Milk Producers Federation

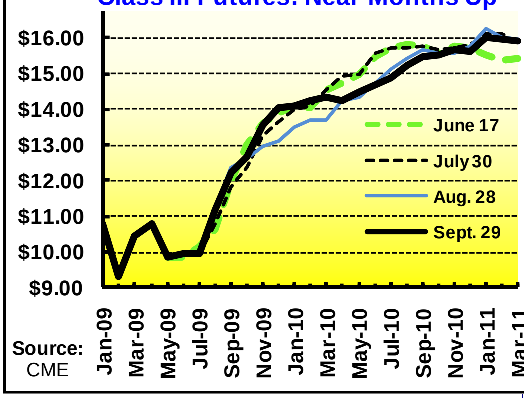
Volume 12, Number 9

Dairy Market Report

Executive Summary

- Cheese, butter prices up from our last report:
  - blocks up 3½¢ to $1.41¼/lb., as of Sept. 30th
  - barrels up 2¢ to $1.36/lb.
  - butter up 6½¢ to $1.23½/lb.
- Commercial disappearance of milkfat down 1% in three mos. ending July; skim solids down 0.6%.
- Outlook: *Shrinking herd and tight powder and cheese markets boost short-term price outlook. Long-term depends on farm survival, exports.*

Class III Futures: Near Months Up



Source: CME

Market Outlook

Dairy markets have strengthened moderately in the last two months, despite mixed signals. Current supplies of milk, nonfat dry milk, and new cheese are tight, thanks to the long-awaited milk reduction coming just as school milk season begins. However, stocks of butter and cheese were large and did not shrink substantially in August. Domestic demand has been boosted by consumer response to lower prices; but exports are off from last year.

The U.S. milking herd was 171,000 cows smaller in August than a year earlier, thanks to crushing bottom lines and accelerated by the CWT program. This reduction was largely off-set by a 1.6% increase in milk per cow; however, the 0.3% year-over-year drop in milk production was the largest in 5 years. The production outlook for 2010 depends on how many farms that survived the storm will also survive the aftermath. USDA's increase in support prices at the beginning of August seemed to have a substantial psychological impact on dairy markets, although more CCC powder sales have been cancelled than contracted since the announcement, and no other products have been sold for support in that time.

Effective risk management ***has become increasingly important to dealing with growing milk price volatility. We have discussed before the ability of many Eastern and Mid-Western farmers to survive the recent milk-feed margin crunch because they hedge their feed cost risk by growing their own feed. Another group of farmers that continue to milk are those of any size or structure that took advantage of high milk futures prices last year to hedge their milk price risk. In June 2008, it was possible to sell Class III milk futures at over $20 per cwt. for every month through December 2009. On August 1, 2008, there was open interest of 7 billion pounds in the Class III contract, equal to about 4% of annual U.S. milk production.***

Cooperatives Working Together (CWT) program announced the completion of its second round of herd retirements begun in 2009: 74,113 cows producing 1.5 billion pounds of milk per year were retired from the national milking herd in August and September. Also, 2,958 heifers were removed. CWT removed 225,783 cows through herd retirement over the last 10 months.

The Milk Income Loss Contract payment rates for September and October are, in effect, final, as the feed cost adjustor will not have an impact on these months. At present, the October payment rate is projected to be the highest of Fiscal Year 2010. dmr

MILC Payment Rates and Projections

Year	Boston Class I Actual	Boston Class I Target	Payment Rate
FY 2009			
October '08	18.78	18.48	0.0000
November	20.58	18.10	0.0000
December	18.68	17.76	0.0000
January '09	18.99	17.98	0.0000
February	13.97	17.33	1.5135
March	12.68	17.14	2.0056
April	13.61	17.14	1.5863
May	14.22	17.48	1.4673
June	13.33	17.42	1.8411
July	13.51	16.94	1.5435
August	13.29	16.94	1.6425
September	14.18	*16.94*	*1.2420*
FY 2010			
October '09	*15.60*	*16.94*	*0.6030*
November	*15.85*	*16.94*	*0.4899*
December	*16.69*	*16.94*	*0.1137*
January '10	*17.28*	*16.94*	*0.0000*
February	*17.42*	*16.94*	*0.0000*
March	*17.57*	*16.94*	*0.0000*
April	*17.66*	*16.94*	*0.0000*
May	*17.60*	*16.94*	*0.0000*
June	*17.78*	*16.94*	*0.0000*
July	*18.01*	*16.94*	*0.0000*
August	*18.22*	*16.99*	*0.0000*
September	*18.52*	*16.98*	*0.0000*

Projections based on futures as of 9/29/2009

The Dairy Market Report is created for Dairy Management Inc.

The Nutshell

Production v. last year:

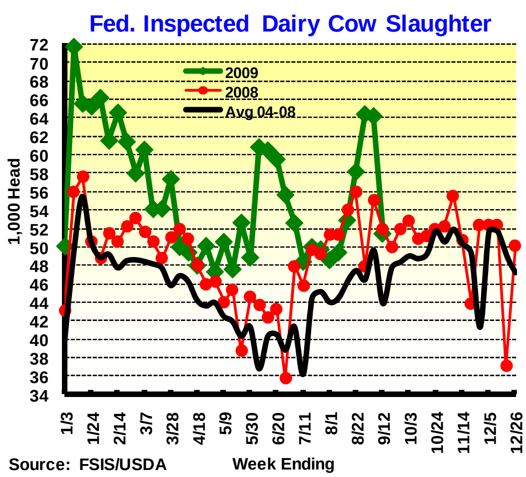
- July Cheese ⬆ 2.0%
- July Butter ⬇ 2.2%
- July NDM+SMP ⬇ 9.8%
- July Whey ⬆ 2.1%
- August Milk ⬇ 0.3%

NASS	July	Aug.
Cheddar	1.13	1.26
Whey	0.29	0.29
Butter	1.20	1.20
NDM	0.84	0.87
Milk	**July**	**Aug.**
Cl. III	9.97	11.20
Cl. IV	10.15	10.38
All	11.10	12.00
September All-Milk:		*12.70*

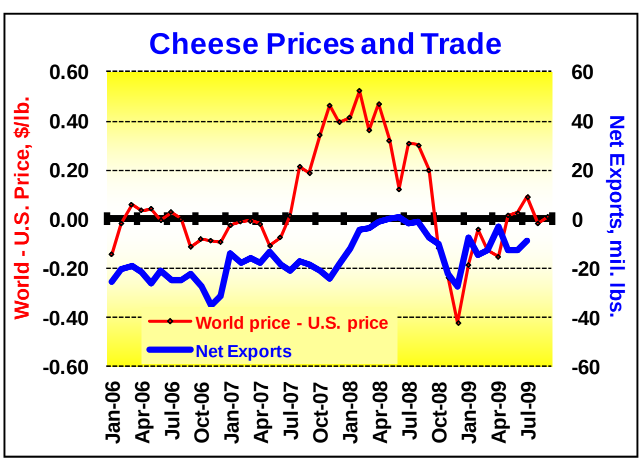
Cheese and Whey

The August cheese stock drawdown was 2½ million lbs., compared to a 10-year average of 35 million lbs.

Total U.S. **cheese** production (excluding cottage cheese) was 839 million lbs. in July, up 2.0% from a year ago; average daily production was down 2.7% from June. American types totaled 352 million lbs. in July, up 3.0% from last year and down 3.5% from June, on an average daily basis. Italian types were 348 million lbs., up 3.1% from last year and down 2.3% from June on an average daily basis. For the year to date, average daily cheese production is up 1.9%.



USDA-reported stocks of American cheese opened September at 621 million pounds, up 9% from last year, and down 7 million pounds from August 1. September's opening stocks of other cheese, including Swiss, were 364 million pounds, up 16% from a year ago, and up 4 million pounds from August. September 1 total cheese stocks were 985 million pounds, up 12% from last year and down only 2½ million pounds from August 1. This compares to a 10-year average 35 million pound August drawdown of total cheese stocks.

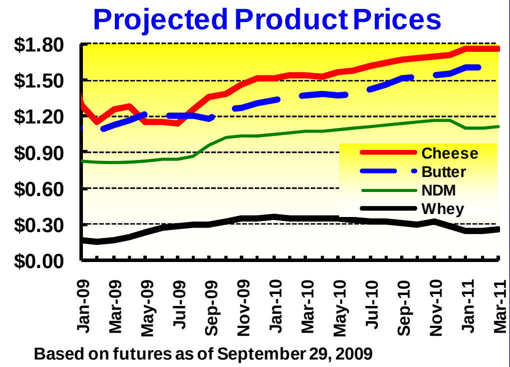


Commercial disappearance for American cheese was 1.04 billion pounds in the three months ending with July, up 4.8% from a year ago. Disappearance of other cheese was up 1.4% to 1.51 billion pounds, and total cheese was up 2.7%.

As of September 30, the CME block cheese price was up 3½¢ per pound from our last report, to $1.41¼; the barrel price was up 2¢, to $1.36. Class III (cheese milk) futures prices have risen in near months, and held steady further out (See graphs, pp. 1, 4.)

September 29 futures project cheese prices to average $1.49 over the next six months (October through March), $1.28 for all of 2009, and $1.61 for 2010.

U.S. cheese exports in July were 21 million pounds, down 13% from a year ago, but still equal to 2½% of U.S. cheese production and about double historical averages. Imports were up 14% from a year ago to 30 million pounds, but somewhat below historical averages. Net imports were 9 million lbs; this is three and a half times the unusually low figure for last July, but also about two-thirds less than the previous 3 July's. (See graph.)



The retail price of cheddar cheese was $4.55 in August (down 6% from last year). Processed cheese averaged $3.90 at retail in August, down 7% from a year ago.

Production of dry **whey** for food was 90 million lbs. in July 2009, up 2% from a year ago. Production of all whey products was up 0.8%. (See box.)

The manufacturers' price of whey was up to 30¢ per lb. the week of September 19, according to NASS' survey. WPC-34 prices are also up, to about 67¢, per USDA's *Dairy Market News*. The CME dry whey futures project average whey prices of 35¢ for the next 6 months, 26¢ for all of 2009, and 33¢ for 2010. The whey price is about 43¢ per lb. in Europe. **dmr**

Whey Products

Product	July Production		August 1 Maker Stocks	
	Mil. lbs.	Change v 2008	Mil. lbs.	Change v 2008
Whey, food	89.6	2.1	46.1	-15.5
Whey, feed	3.7	-1.2	1.7	-70.8
WPC25-51	22.9	-12.1	22.3	-27.7
WPC50-91	12.0	11.8	14.1	-2.1
WPI90+	4.5	35.7	n/a	n/a
Total	***132.7***	***0.8%***	***84.3***	***-20.3%***

Butter

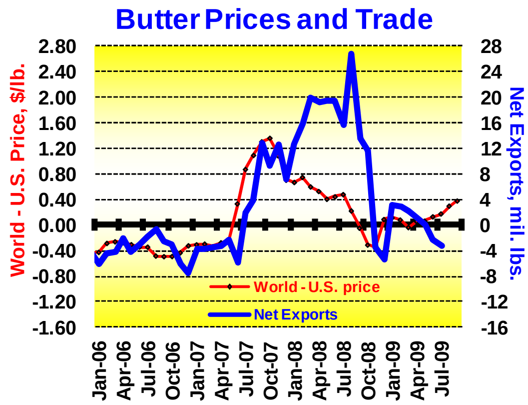
July U.S. butter production was 112 million lbs., down 2.2% from a year ago and down 14% from June, on an average daily basis. Year-to-date production is down 0.4%. September 1 stocks were 263 million pounds, up 23% from a year ago and up slightly from August.

Commercial disappearance for butter (including exports) in the quarter ending with July, was down 2.4% from a year ago and disappearance of all milkfat was down 1.0%.

The retail butter price was $2.77 per lb. in August 2009, down 15¢ from last month and down 9% from 2008. The CME butter price was up 6½¢ since our last report to $1.23½ on September 30. Futures project NASS butter at $1.32 for the six months through March, $1.19 for all 2009, $1.44 for 2010.

U.S. net butter imports in July were 3.2 million lbs., compared to net *exports* of 15.7 million lbs. last July.

In just the first 3 months of the July to June marketing year, USDA has already awarded DEIP bonuses for 25 million of the 47 million pounds of the supported exports allowed under WTO rules. Butter in Oceania is about $1.05 per lb., according to USDA's international report, compared to European prices of about $1.60. **dmr**



Dry Milk Powders

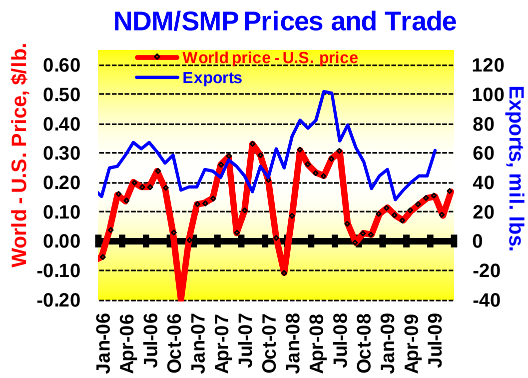
U.S. nonfat dry milk production, including protein-standardized "skim milk powders" was 146 million lbs. in July, down 9.8% from a year ago. August 1 manufacturers' stocks of (only) nonfat dry milk were 172 million lbs., up 12% from last year, and down 23 million pounds from July 1.

Since our last report, the CME price of extra grade nonfat dry milk was up 20¢ to $1.15 per lb., and grade A was up 15½¢ to $1.15, on September 30; this compares to the average surveyed U.S. manufacturers' price of 98½¢ for the week of September 19.

In July 2009 exports of nonfat dry milk and skim milk powders were 62 million pounds, down 9% from last July's total, but the largest total since last September.

There have been no DEIP awards since September 3, as world prices have risen above U.S. prices. Export bonuses have been awarded for 38 million pounds of nonfat dry milk out of the 150 million pounds allowed under world trading rules in the July to June marketing year.

USDA purchases of nonfat dry milk under the price support program have come to a near stop, despite the temporary increase in the support price to 92¢. There have been no net sales to CCC since the end of July, as U.S. and world prices have risen.



Commercial disappearance of nonfat dry milk (including exports, but excluding modified "skim milk powders") were 391 million lbs. in the three months ending July, up 0.6% from a year ago; and all skim solids was down 0.6%. **dmr**

Yogurt, Ice Cream, and Fluid Milk

U.S. yogurt production in July was up 6% from last year, to 304 million lbs; year-to-date was up 7%.

July's reported ice cream production was up 2% from a year ago, to 127 million gallons, and down 0.8% for the year to date. Ice cream mix production was 71 million gallons, up 0.2% from a year ago, and down 0.3% for the year to date.

The retail ice cream price was $4.28 per ½-gallon in August, up 1% from last year.

Fluid milk sales for June were up 2.2% from a year ago (calendar-adjusted), when the retail price of whole milk was down 24%. August's retail price was $2.98, down 23% from a year ago. **dmr**

U.S. Fluid Milk Sales

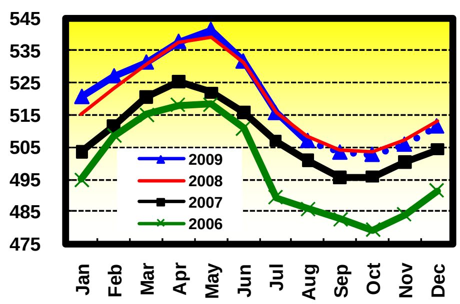
	July 2009		2009 to date	
Product	Mil. lbs.	%	Mil. lbs.	%
Whole Milk	1,279	1.8	8,724	-0.6
Flavored Whole Milk	47	-1.3	334	-1.9
Organic Whole Milk	31	7.1	214	-0.4
Reduced Fat Milk (2%)	1,554	3.7	10,716	1.8
Low Fat Milk (1%)	527	3.8	3,933	2.5
Fat-Free Milk (Skim)	665	1.0	4,723	-0.4
Flavored Fat-Reduced	149	4.6	2,147	3.6
Organic Fat-Reduced	102	5.6	707	-3.4
Buttermilk	41	2.0	378	17.3
Total (including "Other")	**4,403**	**2.7**	**31,931**	**0.9**
Total (calendar adjusted)	**4,368**	**2.2**	**31,881**	**1.3**

Source: USDA/AMS, Dairy Market News

Milk and Feed

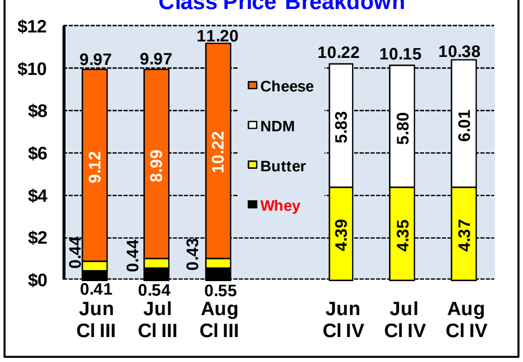
U.S. milk production in August was 15.7 billion lbs., down 0.3% from a year ago. Milk per cow was up 1.6%, but ***the herd was 171,000 cows (1.8%) smaller than a year ago***. This year-over-year decline

U.S. Milk Production, 2006-2009
Million Lbs./Day



should grow through August and September, as CWT's removal of 77,000 cows and heifers in its most recent round of CWT herd retirements shows up in the USDA herd numbers. (See slaughter graph on p. 2.) Production has been up 0.2% in the first 8 months of 2009, on an average daily basis. USDA projects a 2.0% decline in the last quarter of the year. The easing of feed prices

Class Price Breakdown



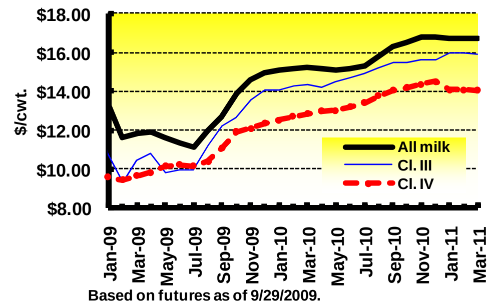
(see below), an ample supply of replacement heifers, a revival of demand after record prices in 2007-2008, and the slow recovery of milk prices all make such a large reduction unlikely, although a reduction as large as 1% should be expected for the rest of the year. (See also p. 1.)

August's Class III price was announced at $11.20 per hundredweight, up $1.23 from July, but down $6.12 from a year ago. Class III futures prices for the next six months (October through March) averaged $13.83 per hundredweight on September 29, and they project averages of $11.23 for 2009 and $14.87 for 2010. September is projected at about $12.20. The Class III price is the minimum price paid for cheese milk pooled on Federal orders.

The August Class IV price was $10.38, up 23¢ from August, and down $6.26 from a year ago. Futures markets project Class IV milk to average about $12.40 for the next six months, $10.57 for 2009, and $13.45 for 2010. September is projected at about $10.70. The Class IV price is the minimum price for pooled milk used to make butter or milk powder.

August component prices were: $1.2491 per lb. (up a ha'penny from July) for butterfat in Class III, Class IV, and producer milk; $2.1009 (up 40¢) for protein in Class III and producer milk; $0.6918 (up 2¢) for total nonfat solids in Class IV milk; and

Projected Milk Prices



$0.0962 (nearly unchanged) for other solids in Class III and producer milk. September butterfat is projected at $1.37.

August's Class II price was down a penny, to $10.86 per hundredweight. This is the minimum price for pooled milk used to make soft dairy products and in most food processing. September is projected at about $11.30.

October's Class I base price was announced at $12.35, up $1.42, based on rising cheese values. The Class I base price plus a location differential is the minimum price processors pay at the plant for bottling milk pooled on a Federal order.

September's all-milk price was $12.70; August's was $12.00, up 90¢ from July (which was the lowest in 6 years). The futures markets project the all-milk price to average $12.60 in 2009 and $15.70 in 2010.

Feed costs are mixed: near month corn and soy futures are $3.41 (up 20¢) and $9.17 (down $2.70) per bushel. Futures markets project 2009 averages for corn at $3.70 ($3.70 in 2010) and soybeans at $9.95 ($9.10 in 2010). **dmr**

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